

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

JOHNSON COUNTY GAS CO., INC.,)	
VAN LEAR, KENTUCKY 41265)	
APPLICATION FOR AUTHORITY TO)	CASE NO. 8235
ADJUST RATES ON AN EMERGENCY)	
BASIS)	

ORDER TO SHOW CAUSE

The Commission on its motion pursuant to KRS 278.250 has investigated and examined the condition of Johnson County Gas Company (Company). The results of that investigation contained in a report to the members of the Commission, dated March 9, 1982, and appended to this Order disclose apparent irregularities in the financial condition and management practices of the Company. Based upon the findings of this investigation, the Commission pursuant to KRS 278.280 has determined that a hearing should be held to determine whether the apparent deficiencies and irregularities do in fact exist, jeopardizing the maintenance of service by the Company and whether specific action is required by the Commission to alleviate these alleged problems.

Upon motion of Johnson County Gas Co., Inc., through its counsel, for an extension of time to prepare its case,

IT IS ORDERED that, contingent upon compliance with the terms of this Order, Johnson County Gas Co., Inc., is granted a continuance of this matter until 1:00 P.M., EDT, April 26, 1982, when it shall appear at the office of the Commission, 730 Schenkel Lane, Frankfort, Kentucky, to show cause by testimony and documentary evidence why:

1. The Commission should not adopt as correct the conclusions contained in the report of March 9, 1982, from Mr. Dell Coleman to the members of the Commission;

2. The president of the company, Mr. Danny Preston, should not be required to restore to the Company any funds paid to and for any business enterprises or interests other than those directly related to the affairs of Johnson County Gas Company;

3. The current financial and management practices of the Company will not lead to deterioration of service to its customers; and

4. The current financial and management practices will not lead to further indebtedness to creditors, and continued default in payment of indebtedness previously incurred.

IT IS FURTHER ORDERED that, by agreement of the parties, during the pendency of this action the Company and its officers shall not dispose or encumber any assets of the Company; shall not transfer any money, property or assets of the Company to its officers; shall not disburse any funds of

the Company except as follows: (1) normal payroll and related state, local and federal tax obligations to its employees, (2) payments to existing gas wholesalers, and (3) other suppliers of goods and services for expenses incurred in the normal course of business; and shall not declare any dividend or other distribution of property to the shareholders.

IT IS FURTHER ORDERED that the Company, through its officers, shall present to the Commission at the time of the hearing in this matter the following documents in addition to any other documents which the Company may provide which indicate sound accounting, financial and management practices by the Company: All evidence of loans made by the president, Mr. Danny Preston, to the Company, deposit slips which show these funds were deposited in a Company account and bank statements which show these funds were credited to the Company's bank account.

Done at Frankfort, Kentucky, this the 18th day of March, 1982.

PUBLIC SERVICE COMMISSION

Marilyn M. Vohz
Chairman

Katherine Randall
Vice Chairman

Don Carver
Commissioner

ATTEST:

Secretary

INTRA-AGENCY MEMORANDUM

KENTUCKY PUBLIC SERVICE COMMISSION

TO: Chairman Volz
Vice Chairman Randall
Commissioner Carrigan

THRU: Richard D. Heman, Jr.
Acting Executive Director

FROM: M. D. Coleman, Director
Division of Rates and Tariffs

DATE: March 9, 1982

SUBJECT: Examination of Johnson County Gas Company's
Books and Records

Pursuant to your request, the staff has performed a limited examination of the books and records of Johnson County Gas Company for the year ended December 31, 1981. The company's general ledger had not been posted since May of 1981. Bank reconciliations were completed and provided subsequent to our arrival. For the foregoing reasons, the scope of the examination was limited to a review of the cash receipts journal and the bank statements, together with the reconciliations and the cash disbursements journal which was posted after our arrival. The results of this examination are based on the limited information available to the staff during the examination and discussions with the company's accountant and its president.

Overview

Johnson County Gas Company serves approximately 884 customers in the community of Van Lear, Kentucky, and the area adjacent thereto. Reconstruction of the system was completed during 1981. Prior to reconstruction, significant line loss was being experienced and the company had accumulated significant accounts payable to its suppliers. As a result of reconstruction, line loss on the system has been reduced to an acceptable level. The company borrowed the funds to reconstruct the system from the Department of Local Government ("DLG"). The total amount borrowed was \$1,321,374. To date, no repayment has been made on the loan and the company's accountants have

asked DLG to postpone repayments on the loan until January 1, 1984. Schedule 1 shows the company's principal creditors, the amount paid these creditors in 1981, and balance owed as of December 31, 1981.

Through January 1982 the company had five employees. Schedule 2 shows that total annual salaries are \$65,400.

Our review of the cash disbursements journal disclosed several questionable expenditures:

Additional Payments to Employees

In July of 1981 each employee received \$300. The notation on the check stub was "vacation-extra work." In December, the employees received three checks (normally would receive two). The notation on the stub of the third check was "Christmas bonus."

Contributions

In December 1981 the company contributed \$500 to a children's home.

Disbursements to Mr. Preston

In November 1981, Check No. 2379 to Citizens Bank for \$5,100 was entered in the cash disbursements journal. This entry was based on the notation on the check stub. Our review of the check disclosed that the payee was the president, Mr. Danny Preston. The company's accountant indicated the funds were used to pay for the option to buy B&H Gas Company. Mr. Preston indicated it was in repayment of a \$10,000 loan he made to the company. It is not clear at this time how the loan was made to the company or whether any funds were actually deposited to the company's account. Our review of the deposit slips did not disclose a deposit for this amount.

In December 1981, Check No. 2428 for \$5,000 was written to cash. The payee listed in the cash disbursements journal is Citizens Bank. The best information we have at this time is that it was a repayment for a loan from Citizens. We are again handicapped because the records are not closed. The company's annual report for 1980 lists notes payable of \$18,445 of which \$1,233 was to Citizens Bank.

Communications Cost

In addition to its regular telephone service, the company pays for a communications service purchased from Ditronics and C & D Towers. The total amount paid in 1981 was \$3,625.50.

Reimbursement For Damage to the System

In 1981, Addington Mining Company had an accident which blew out a part of Johnson County's line. Johnson County settled with Addington for \$15,340. Mr. Preston deposited \$15,000 in the company's account and retained \$340. The company then wrote Check No. 2373 to Mr. Danny Preston for \$15,000. According to Mr. Preston, he had mortgaged his house for \$25,000 and loaned this amount to the company. Our review did not disclose any deposit of this amount to the company's account. The company's accountants have indicated that payments to Mr. Preston over and above his salary will be treated as loans.

The staff also reviewed the company's monthly billing, cash receipts and delinquent journals relating solely to customer accounts. Our review of these journals indicates the company has severe problems in its customer collections. Schedule 3 provides a summary by month of the billings from January 1981 through January 1982. This schedule shows the service period of the bill, date the bill is due, the amount of current past-due and total billings and the percentage of past-due to current billings. As the schedule shows, past-due to current billings range from a high of 225.68% in August 1981 to a low of 25.08% in January 1982. During this period, past-due billings were on average 50.18% of current billings.

It is our opinion from this analysis that the company clearly has severe collection problems. From our discussions with the company's accountants and Mr. Preston, this problem seems to arise from two sources. According to Mr. Preston, during the first part of 1981 miners were having a difficult time paying their bills as a result of the strike. During the last half of 1981 this problem appears to stem from a dispute between the company's president and some of its customers over the effective date of the company's last rate increase. We believe that a significant number of customers currently distrust the company's management. Good customer relationships are essential to a utility's operations. This relationship is management's responsibility. However, because we perceive the problem to

be serious, the Commissioners may want to consider a town meeting in March to explain why the last rate increase was necessary and the consequences to the customers of their refusal to pay.

From this preliminary review of the company's financial records, the Commission's file and the above noted discussions, the staff does not believe the company is being managed prudently. The staff's conclusions are based on the following reasons:

1. There has been little or no planning by the company to meet its obligations to its creditors. In the last couple of months, the company's accountants have contacted most creditors to try and arrange a repayment schedule.
2. The company has too many employees. The system has just been rebuilt, maintenance has been and should be minimal. Accordingly, it would seem reasonable to pay a contractor a retainer in case of an emergency and eliminate all but two employees.
3. The company president has little or no financial expertise and must rely totally on his outside accountants even to the point that they are required to establish a repayment plan for past due amounts owed creditors. The accounting firm is reluctant to do work for a client whose credit worthiness is questionable. While we understand that no company's records for 1981 would be closed in January of 1982, the condition of this company's records is inexcusable. The company will incur substantial cost in getting its records updated and closed in 1981.
4. Mr. Preston, as president of the company, claims certain loans were made to the company. This is questionable since deposits representing these loans to the company could not be identified from the bank statements. This cannot be completely verified until the records are closed.
5. Recorded payees on check stubs and in the disbursements ledger do not agree with the payee on the check. These amounts are significant, considering this company's cash flow problem.

6. The number of vehicles owned by this company appears unreasonable for its size, and equipping them with two-way radios does not appear prudent, in our opinion, since ordinary methods of communication would suffice.
7. The customer relationship is seriously damaged as a result of the last rate increase being billed prior to its effective date. Much of this could have been avoided if the company had heeded the letter from Secretary Heman, or had made the refund in the next month on a voluntary basis. Public statements by the company president to the effect that no refund would ever be made have only served to strain the relationship further.

There is serious question, in our opinion, as to the ability of the existing owner to maintain this system on a sound financial basis. The company has indicated its records will not be closed for 1981 until April 15, 1982. If we assume adequate documentation exists for certain questionable transactions, we would estimate two weeks in the field, another week to prepare the draft and a week to finalize the draft. Therefore, we believe a final report could be issued by the middle of May.

MDC/cs

Attachments

JOHNSON COUNTY GAS COMPANY, INC.

Schedule of Accounts Payable
As of 12-31-81

<u>Creditor</u>	<u>Amount</u>	<u>Negotiated Payment Terms</u>
Department of Local Government	\$1,321,374.00	Trying to set two(2) year deferral
Columbia Gas, Inc.	138,197.66	
Kentucky-West Va. Gas Co.	31,888.66	
Small Business Administration	23,000.00	
Helton, Butler & Wells	19,380.42	
Howes Johnson	9,500.00	
Internal Revenue (941)	8,136.06	
General Motors	5,025.72	\$239.32 Per Month
Reams Control	5,334.19	\$500.00 Per Month
Heath & Associates	2,578.98	
Citizens Bank	2,486.01	\$828.67 Per Month
Consolidated Pipe & Supply	2,191.16	
Amps Products	1,121.68	\$100.00 Per Month
Phillips Engineering	883.09	\$100.00 Per Month
Fisher Controls	811.81	\$100.00 Per Month
Doug's Gulf	789.62	
Aetna (Workmens Comp.)	513.00	
C & D Tower Service	257.00	
Graphic Controls	40.91	
Ollwell	29.29	
Paintsville Herald	26.37	
Total	\$1,573,565.63	

JOHNSON COUNTY GAS COMPANY, INC.

Schedule of Employees
As of 12-31-81

<u>Name of Employee</u>	<u>SS Number</u>	<u>Annual Salary</u>
1) Bobby Goble	403-96-8960	\$ 9,600
2) Suzanne Watkins	401-58-5936	7,200
3) Betty Preston	284-48-8386	9,600
4) Danny Preston	402-64-1072	27,000
5) Kerby Goble	406-82-2619	<u>12,000</u>
Total Annual Salaries Expense		\$ 65,400

Duties

- 1) Bobby Goble - Assistant Field Manager - Field Work & Meter Reading
 - 50% Mains & Service Labor } Test Period
 - 50% Meter Reading Labor }
 - 80% Mains & Service Labor } Projected Period
 - 20% Meter Reading Labor }
- 2) Suzanne Watkins - Secretary
 - 50% Accounting & Collecting Labor } Test Period
 - 50% Admin. & General Labor }
 - 75% Accounting & Collecting Labor } Projected Period
 - 25% Admin. & General Labor }
- 3) Betty Preston - Corporate Secretary, Treasurer, & Office Manager
Same as Suzanne Watkins
- 4) Danny Preston - Chief Executive Officer & Operations Manager
100% Supervision
- 5) Kerby Goble - Field Manager - Field Work & Meter Reading
Same as Bobby Goble

JOHNSON COUNTY GAS COMPANY, INC.

Summary of Monthly Billings to Customers
Due for the Months of January 1981
Through February 1982

Service Period Current Usage (a)	Due Date of Total (b)	Current Billing (c)	Past-Due Billings (d)	Total Due (e)	Past-Due % of Current (f)
11-27-80 to 12-26-80	1-26-81	\$ 43,039.90	\$ 12,087.17	\$ 55,127.07	28.08
12-27-80 to 1-15-81	2-19-81	54,523.95	18,844.21	73,368.16	34.56
1-16-81 to 2-15-81	3-15-81	52,669.26	23,487.44	76,156.70	44.59
2-16-81 to 3-15-81	4-15-81	35,180.20	21,622.13	56,802.33	61.46
3-16-81 to 4-15-81	5-15-81	25,487.71	19,599.92	45,087.63	76.90
4-16-81 to 5-15-81	6-15-81	16,498.97	21,214.62	37,713.13	128.58
5-16-81 to 6-15-81	7-15-81	10,187.88	17,679.83	27,867.71	173.54
6-16-81 to 7-15-81	8-15-81	7,242.45	16,344.50	23,586.95	225.68
7-16-81 to 8-15-81	9-15-81	7,648.01	14,037.40	21,685.41	183.54
8-16-81 to 9-15-81	10-15-81	8,506.51	12,996.85	21,503.36	152.79
9-16-81 to 10-15-81	11-15-81	27,502.17	12,061.14	39,563.31	43.86
10-16-81 to 11-15-81	12-15-81	50,257.34	16,166.05	66,423.39	32.17
11-16-81 to 12-15-81	1-15-82	87,693.71	21,989.48	109,683.19	25.08
12-16-81 to 1-15-82	2-15-82	101,264.58	36,692.23	137,956.81	36.23
Total Billings		<u>\$527,702.64</u>	<u>\$264,822.97</u>		<u>50.18</u>